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Business-Friendly Decisions on Size Appeals

By Patrick T. Rothwell

Several size appeal decisions recently issued by the U.S. Small Business Administration's Office of Hearings and Appeals (OHA) are of interest to contractors pursuing set-aside procurements. The common thread in these size decisions is that OHA appears to be taking a more practical approach to the business arrangements between small business contractors and other businesses. That means small businesses may be somewhat less likely to be the subject of an adverse size determination. Three decisions summarized below are indicative of this trend.

In *Size Appeal of Trident³ LLC*, SBA No. SIZ-5315 (2012), OHA significantly limited the ability of protesters to challenge the substance of 8(a) mentor-protégé joint venture agreements that have received prior SBA approval. OHA held that SBA area offices may *not* review the substance of such agreements for compliance with SBA regulations. This case overruled prior case law in which OHA held that an SBA area office was obligated to review 8(a) joint venture agreements for compliance with SBA regulations.

The result is that size protests can no longer challenge a joint venture's compliance with the 8(a) joint venture rules, or the size of the two parties in the joint venture, for 8(a) contracts. This puts added emphasis on SBA to ensure it properly reviews and approves of joint ventures for 8(a) contracts, including by verifying the size of the parties in the joint venture.

Notably, non-8(a) set-asides were beyond the scope of *Trident³*. Therefore, joint ventures that pursue non-8(a) set asides presumably will still be subject to review by SBA area offices in size protests, since such joint ventures are not pre-approved by an SBA district office.

Next, in *Size Appeal of Nuclear Fuel Services, Inc.*, SBA No. SIZ-5324 (2012), OHA signaled that it may now be taking a more flexible approach in determining when an "agreement in principle" has been reached. SBA size regulations provide that agreements for a merger or acquisition, including agreements in principle to merge, have a "present effect" on the power to control a concern. 13 C.F.R. § 121.103(d)(1). This means that, in a size protest, the effective date of the merger is the date that an "agreement in principle" is reached, even if it is before the date of the actual merger.

Difficulties in identifying an "agreement in principle" increase the risks that contractors pursuing mergers while simultaneously pursuing set-asides could run afoul of the "present effect" rule, if size protested.

In *Nuclear Fuel Services*, OHA reversed an SBA area office finding that a large firm's merger offer letter outlining specific terms constituted an "agreement in principle." Among the details in this letter were terms, such as price, and other conditions.

Contrary to the area office, OHA found that the above-referenced letter did not establish the existence of an "agreement in principle" even though the letter included terms such as price, and the deal was ultimately consummated several months later. OHA found that the letter did not constitute a meeting of the minds between the parties because it did not indicate that the seller accepted the proposal.

Finally, OHA provided new guidance on the application of the ostensible subcontractor rule in Size Appeal of *Spiral Solutions and Technologies, Inc.*, SBA No. SIZ-5279 (2011). An "ostensible subcontractor" is a subcontractor that either performs the primary and vital requirements of a contract or task order or is a subcontractor upon which the prime contractor is unusually reliant. If SBA finds that there is an "ostensible subcontractor," the prime contractor and the subcontractor are treated as affiliates for size purposes.

Seemingly contrary to past decisions, OHA held in *Spiral Solutions* that the ostensible subcontractor rule was not violated when neither the proposal nor the teaming agreement assigned discrete tasks to the subcontractor, but only assigned percentages of work to be performed by both parties. OHA also determined that the repeated use of "team" language and "team" logos in the proposal did not indicate that the prime contractor was unusually reliant upon the subcontractor.

And, while prior ostensible subcontractor cases had found the prime contractor's hiring of the subcontractor's incumbent, non-management personnel to be a factor in affiliation, OHA held in *Spiral Solutions* that this no longer made sense in light of the rules requiring the successor contractor to give a right of first refusal to incumbent personnel.

The bottom line from this decision is that OHA seemed to go out of its way to find that the arrangements between the prime and the subcontractor did not run afoul of existing precedent on the ostensible subcontractor rule, suggesting that OHA might give small business contractors greater leeway in their teaming arrangements with larger companies than in the past.

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